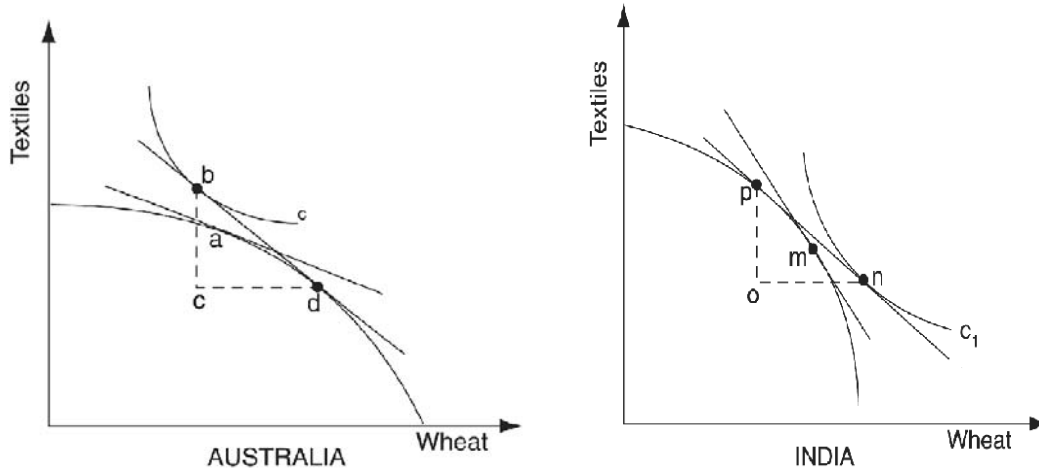


Neoclassical and Heckscher-Ohlin Model: Practice Problems

International Trade

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Question 1 Consider the following international trade equilibrium between Australia and India:



- What must be true about the relationship between the prices, costs, and utility associated with consuming and producing textiles and wheat in autarky at point m in India?
- What must be true about the relationship between the prices, costs, and utility associated with consuming and producing textiles and wheat at point p in India?
- Which country has a comparative advantage in wheat?
- What quantity of goods does India export?

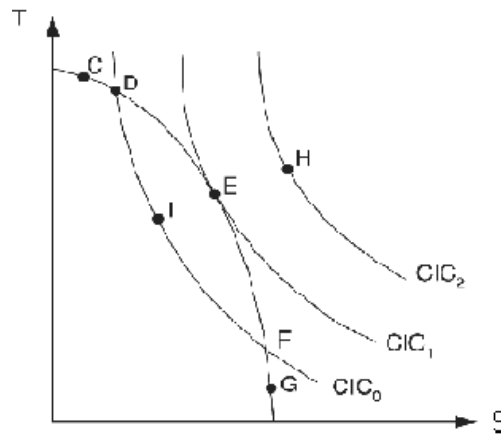
Question 2 Consider the simple Heckscher-Ohlin model discussed in class. You are given the following data on the factor endowments of two countries, A and B:

	Country A	Country B
Labor Force (millions of workers)	45	20
Capital Stock (thousands of machines)	15	10

- Which country is relatively capital abundant? Explain.
- Which country is relatively labor abundant?

- c) Suppose that steel is capital intensive relative to T-shirts. Which country will have comparative advantage in the production of steel? Explain.
- d) Which factor benefits the most in country B under international trade? Why?
- e) Under what circumstance might factor price equalization not occur when countries A and B trade?

Question 3 Answer the following questions based on the diagram below.



CIC refers to the country's indifference curve.

- a) In autarky, the economy would be in general equilibrium at point
 - a. I
 - b. D
 - c. E
 - d. F
- b) Which of the following is true?
 - a. The relative price of S is higher at G than at D.
 - b. The relative price of T is higher at C than at F.
 - c. A move from C to D would raise country welfare.
 - d. All of the above are true.
- c) In the autarky equilibrium, the relative price is given by the slope of the production possibility frontier at point
 - a. D
 - b. E
 - c. F
 - d. Can't answer without more information.

Question 4 According to the Heckscher-Ohlin (HO) model, the source of comparative advantage is a country's

- a. Technology
- b. Advertising
- c. Factor endowments
- d. Both a. and c.

Question 5 The HO model rules out the Ricardian model's basis for trade by assuming that _____ is (are) identical between countries.

- a. Factor endowments
- b. Factor intensities
- c. Technology
- d. Opportunity costs

Question 6 Suppose there are two factors, capital and land, and that the United States is relatively capital abundant while Canada is relatively land abundant. According to the HO model,

- a. Canadian landowners should support Canada-U.S. free trade.
- b. Canadian capitalists should oppose Canada-U.S. free trade.
- c. U.S. capitalists should support Canada-U.S. free trade.
- d. All of the above.